6/2/80 B 4750-1

Financial Markets

Irving Trust

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Friday April 18, 1980

"Yes, but--" was the message from the financial markets, as an extraordinarily hectic week drew to a close. Yes, the long-awaited cyclical peak in interest rates has passed (market consensus on that point reached near-unanimity this week); and yes, the U.S. economy has moved into recession, indicating that a major cyclical downtrend in rates has begun and will continue. But--and here the focus shifts from the medium term to the immediate future--cyclical trends are seldom smooth, and many market watchers feel that swings around the underlying downtrend may be sharper this time round than they have been in the past.

Fixed income markets--most spectacularly the governments sector--boomed ahead this week, despite a widely held suspicion that a reversal is bound to take place in the not-too-distant future. Markets were hesitant early in the week, but a massive rally exploded on Wednesday, as a prime rate cut by a major New York City bank and a statement by a noted money market economist put the seal on the market's assumption that interest rates have peaked.

Wednesday's gains were notable, to say the least. The U.S. Treasury long bond (due 2010) rose in price from 102 (yielding 11.51%) to 108 (yielding 10.80%); on February 28, this issue was priced at 90.625 to yield 13.00%, and yields on other Treasury issues skidded by up to 100 basis points. Thursday saw some consolidation, but prices began to rise again on Friday after the Federal Reserve took action which could point to policy easing. Price movements in corporate and municipal markets were less dramatic (trading remains very thin); but for the first time in weeks, some new issues were pushed ahead of schedule, not delayed.

Now, the question is how long can the rally last--not the cyclical rate decline that is in place on economic fundamentals, but the specific market reaction that has pulled up prices so sharply in recent weeks. That reaction has been so sharp as to create a technically overbought condition, leaving the market vulnerable to a big correction. If that correction is to be avoided, the market needs a continuing diet of good news--more signs of a softening economy and softening credit demands, more signs of potential inflation relief, and (most important) more signs that the Fed will not stand in the way of downward movements in market rates.

In these circumstances, markets will be particularly sensitive to news items over the next few weeks, and rates could move sharply. It is too soon to expect statistical signs of easing inflationary pressures, and a good deal of recessionary economic news is assumed in current market levels. Thus two factors will be of key importance: money supply data (an indicator of credit demands), and Federal Reserve actions. The widely expected April money bulge has not yet appeared; that could come this afternoon or next Friday. As to the Fed, markets will follow very closely the balance it strikes between appropriate accommodation to interest rate declines on the one hand, and inflationary and foreign exchange market considerations on the other.

Anne Parker Mills

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Market Yields

	4/18/80	Week Ago	Year Ago
Prime Lending Rate at Irving Trust Company	(noon)		
Short-term loans to substantial depositors with highest credit rating	19.50%	20.00%	11.75%
Effective since	4/18/80		
Discount Rate at Federal Reserve Bank	13.00/16.00	13.00/16.00	9.50
Federal Funds	18.50	19.00	10.00
Repurchase Agreements	16.00	18.00	9.45
U.S. Treasury Issues			
Bills			
3 months	14.20	14.50	9.65
6 months	13.70	14.90	9.98
1 year	13.00	14.10	9.96
Coupons			
2 years	12.40	13.12	9.75
4 years	11.90	12.25	9.27
7 years	11.26	11.70	9.18
10 years	11.33	11.70	9.16
Long Bond	11.16	11.47	9.07
Negotiable Certificates of Deposit-Secondary Market			
1 month	16.75	17.55	9.80
3 months	16.30	17.50	9.90
6 months	17.65	17.10	10.19
1 year	N/A	N/A	10.25
Banker's Acceptances			
1 month	16.60	17.40	9.77
3 months	16.55	17.45	9.99
6 months	15.40	17.15	10.25
Eurodollar Deposits			
1 month	17.69	18.75	10.31
2 months	17.63	18.81	10.38
3 months	17.44	18.81	10.50
Commercial Paper - Prime Names			
Directly placed by:			
Finance Companies			
1 week	12.00	12.00	6.00
1 month	15.00	17.25	9.38
3 months	13.00	15.00	9.63
Bank Holding Companies			
1 month	15.75	17.75	9.25
Dealer Placed:			
3 months	15.80	16.50	9.63
New AA Corporate Utility Bond	14.25	14.40	9.85
Tax Exempt			
6 month Project Notes	6.75	7.25	5.20
1 year AAA Bond	6.50	7.00	N/A
5 year AAA Bond	6.50	7.10	N/A
20 year AAA Bond	7.30	8.00	5.85

This information represents prevailing market yields.
It should not be construed as an offering.
All yields are on the offered side of the market.

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